TESTIMONY OF
HARVEY L. PITT, CHAIRMAN
U.S. SECURITIES AND EXCHANGE COMMISSION

CONCERNING THE STATE OF THE NATION'S FINANCIAL MARKETS IN THE WAKE OF RECENT TERRORIST ATTACKS

BEFORE THE COMMITTEE ON FINANCIAL SERVICES

UNITED STATES HOUSE OF REPRESENTATIVES

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Chairman Oxley, Ranking Member LaFalce, and Members of the Committee:

I am pleased to appear before you on behalf of the Securities and Exchange Commission to testify on the state of the Nation's securities markets in the wake of the recent terrorist attacks in New York and Washington.

September 11th was a terrible, dark day. The terrorists who attacked our Nation's Capital and the World's Financial Capital, inflicted irreparable losses of innocent lives and caused untold physical damage; but they did not destroy or diminish our Nation's strength, courage or resolve. We grieve for our lost friends and relatives; yet the Nation's response to this catastrophe has been extraordinary.

When tragedy struck two weeks ago, our Nation responded by coming together. Police, firefighters, emergency medical personnel, members of the military and civilians participated in rescue efforts to save those injured in the attacks. This same spirit of cooperation imbued the tremendous efforts by so many in the private and public sectors to restore the vitality of all of our securities markets. By Monday September 17, all the Nation's securities markets resumed trading – less than one week after these heinous attacks –a trenchant message to the perpetrators.

As the events of the last two weeks demonstrate, our capital markets are the world's strongest and most resilient. It is not possible to destroy them physically. Our free markets are not located in any one building or city or place. They are an amalgamation of people and ideas and freedom. They are emblematic of our great Nation. Accordingly, getting our markets back up and running was critical to the recovery effort.

An attack of this nature and magnitude cannot be viewed in a vacuum. We coordinated our efforts with the larger federal government of which we are a part, and we worked cooperatively with the industry we oversee. We at the SEC had two critical roles: first, to assist in implementing national policy; and second, to facilitate the responses planned by the securities industry, and ensure that those responses were consistent with the protection of investors and the national interest. We sought to provide certainty – to facilitate the reopening of fair and orderly markets, and to restore public confidence.

In times of crisis, we believe strongly that our obligation is to keep all those with a role as fully informed as possible. Upon learning of the World Trade Center disaster, we established communications with the organized securities markets and participated in frequent telephonic meetings of the President’s Working Group on Financial Markets. In addition, we provided information to the White House and members of our House and Senate oversight committees.

Immediately following the attacks of September 11, we, together with our colleagues from Treasury, arranged to meet in Manhattan with the leadership of major markets, securities firms, banks, and clearing agencies, along with the offices of the Governor and Mayor, Con Edison and Verizon, and the New York Fed, to assess the situation and determine readiness for a reopening of the markets. Our role in arranging these meetings was not to dictate a decision, but to facilitate a market solution. We held daily joint press conferences to keep the public fully and timely advised.

The decision on when to reopen the markets was made by the private sector -- the markets and major market participants -- in consultation with the Commission. At meetings on Wednesday, September 12, and Thursday, September 13, this group unanimously agreed that, while every effort should be made to reopen the markets as soon as possible, there should be no interference with rescue efforts or jeopardy to securities industry personnel returning to work. Additional considerations included whether there would be adequate and reliable electric power and telecommunications services. Connectivity among various market participants was a significant concern. As a result, the industry representatives unanimously decided that the fixed income markets and futures markets should resume trading on Thursday, September 13, and equities and options markets on Monday, September 17. Having participated in the discussions that produced these decisions, our agency was confident the right decisions were reached under these extraordinary circumstances.

On Thursday, September 13, the fixed income markets and futures markets successfully resumed trading. Although trading was relatively light and the number of market participants smaller than usual, no major problems were reported. When connectivity problems with clearing banks affected the government securities clearing agency, we closely monitored these problems in conjunction with the Federal Reserve.

Deferring the resumption of equities and options trading until Monday, September 17, permitted extensive testing by market participants of systems operability and connectivity. Throughout the weekend, Commission staff worked with market and industry participants to monitor and coordinate extensive systems testing by the exchanges, clearing agencies and market participants. Fortunately, only minor problems arose and those were readily resolved. The tests ultimately verified that all systems were sound and operational. We wish to acknowledge the invaluable assistance we received from FEMA, the Mayor's Office of Emergency Management, and New York State officials in assuring that market participants needing electrical or communications services received appropriate priority. They also kept us apprised of their assessment of the structural integrity of damaged buildings in the financial district.

From a regulatory perspective, the Commission reached out to major market participants, both directly and through industry groups such as the Securities Industry

Association and the Bond Market Association, to determine whether it could provide appropriate temporary regulatory relief to facilitate the reopening of fair and orderly markets. As a result, the Commission for the first time invoked its emergency powers under Securities Exchange Act Section 12(k) and, on Friday September 14, issued several orders and an interpretive release to ease certain regulatory restrictions temporarily. Last Friday, September 21, we extended this relief for an additional five business days.

A cornerstone of this relief was facilitating the ability of public companies to repurchase their own shares, thereby providing greater liquidity. Specifically, the Commission, for ten business days following the resumption of trading on September 17, has permitted issuers to repurchase their securities without meeting the volume and timing restrictions that ordinarily would apply under our Rule 10b-18 safe harbor, and to do so without adverse accounting consequences under pooling of interests provisions. Announcements by major public companies of significant buy-back programs followed soon after. We also permitted directors, officers and ten percent shareholders to repurchase shares of their companies without certain restrictions contained in Section 16(b) of the Exchange Act. We allowed brokerage firms to calculate net capital without considering days the markets were closed. We provided flexibility to mutual funds to borrow from and lend to related parties.

We also responded to physical ramifications of the World Trade Center attacks. We provided temporary relief permitting Amex specialists to function like floor brokers under certain conditions due to space limitations caused by the Amex's temporary relocation to the NYSE floor. We issued an interpretive release permitting accounting firms to provide bookkeeping services to, and help recover records for, audit clients with offices in and around the World Trade Center. To facilitate mutual fund board meetings, we relaxed in-person meeting requirements.

While we broadly solicited and considered suggestions for appropriate temporary relief, we did not implement all suggestions we received, such as prohibiting all short selling, moving to ten-cent quotation increments, and extending settlement cycles in the equity and corporate debt markets. We did, however, take action -- not intervention -- wherever we could to be responsive to industry concerns and to facilitate a smooth reopening of the markets.

We also made ourselves accessible to investors and market participants. We believe that government is and must be a service industry. The SEC placed additional information for investors and market participants on our website regarding market recovery efforts. Investors were invited to e-mail questions to our staff at our hot line, help@sec.gov. We established a special toll-free investor telephone line. For the first time in our history, we also established dedicated telephone lines for inquiries from market participants and for firms seeking additional relief, and received over 100 calls each day last week. We will continue to staff these hotlines as long as necessary. We want to do anything we can to assure industry participants that, if they come to us with their problems, we will work with them to find solutions, without after-the-fact recriminations, except in cases of venal conduct.

On Monday September 17, all U.S. securities markets resumed trading without incident. The markets did not give way to panic selling. They simply did what they do best: they assessed, and responded to, the crisis rationally. Unlike human beings, capital markets are capable of absorbing great shocks quickly. Last week, our markets also absorbed a tremendous volume of trading.

As an agency, our job is to ensure that our markets are functioning properly so investors can exercise their freedom to buy or to sell. We do not preside over the direction of the markets. That measure is left squarely to investors, whose confidence in the markets we seek to ensure. Although uncertainty existed in our economy before the attacks of September 11th, current indicators show that the American people are ready and willing to use their energies and full resolve to prove that terrorists cannot destroy our Nation's spirit. I am optimistic that investors will recognize this long-term potential and job creation, and that markets will reflect it.

Since trading resumed, our staff and we have continued monitoring developments and assessing the situation. We have continued to make ourselves available to the markets and market participants to address any regulatory issues that arise and to ensure that America's investors once again can rely upon the strength and soundness of our markets. Last Friday, September 21, we took additional actions in response to concerns from market participants. As I mentioned earlier, we extended for five business days – that is, until this Friday, September 28 - the temporary relief that we previously granted.

We also issued three exemption letters to be accommodating of certain regulatory filings and their deadlines. The first letter, to The Nasdaq Stock Market, Inc., changes a deadline under Exchange Act Rule 11Ac1-5, adopted last year. That rule requires market centers that trade national market system securities to report monthly on the quality of trade executions. The first reports for Nasdaq securities, originally due in September, are now due by November 30, 2001, and will cover October trades. We also extended a deadline for reports from broker-dealers on order routing practices. The first reports, for the quarter July through September 2001, will now be due in November 2001. Finally, we granted an exemption from the same order-routing reports to small broker-dealers.

Additionally, we issued an interpretive release explaining how the market closures of the week of September 11 affect the application of two Commission rules. The two rules are Securities Act Rule 144(e), which governs how many shares of stock a corporate insider can sell in the open market, and Securities Exchange Act Rule 10b5-1, which allows people to trade securities pursuant to a pre-existing plan even though they subsequently may learn nonpublic information. Rule 144(e) requires insiders to calculate the average weekly reported volume of trading. The release allows insiders to ignore the week of September 11 in making that calculation. The release also gives insiders greater leeway concerning written plans to purchase or sell securities.

The measures that the Commission adopted pursuant to its emergency authority expire at the end of this week. Before they expire, the Commission will assess whether they are still useful under current conditions. Where appropriate, the Commission will act – either under its emergency authority or pursuant to other authority – to keep these measures in place. We are monitoring the markets closely, and have solicited the input of market participants, to see if there is a need to extend these measures or for additional relief. The Commission is considering whether we should take additional steps to ensure that our markets remain orderly, to remove regulatory measures that, in light of current conditions, inappropriately slow down the capital raising process, and to further the program recently enacted by the Congress to assist distressed industries. We are exploring all possibilities. We appreciate the strong support of Congress for the actions we have taken in the wake of this tragedy. Should we conclude that our efforts to respond to this attack or other major market disturbances would be enhanced by additional authority in these or other areas, we will of course promptly let Congress know.

As you know, our Northeast Regional Office at 7 World Trade Center was destroyed in the aftermath of the attacks. To our tremendous relief, every one of our employees has been accounted for and is safe. Like many affected businesses, however, we now must begin the process of rebuilding. As a first step, the Commission has been supplying the Administration with information it needs to allocate the $40 billion appropriated in H.R. 2888, the emergency supplemental spending measure Congress passed immediately after the attacks. The Commission's needs are many. Most obviously, we will need to relocate and rebuild our Northeast Regional Office. No less important, we must mitigate the effects of these attacks on our regulatory program, and be as prepared as we can for any future attacks. I am deeply grateful to you for your support of this emergency legislation.

As far as the work of the Northeast Regional Office is concerned, we have moved quickly to get things back on track. Within two days of the attack, we had retrieved all documents stored electronically and had commenced a review of every single investigation and case currently underway in the office with the twin aims of ensuring that we do not miss any imminent deadlines and of developing a plan for completing our investigations and cases in timely fashion. While our review has not been completed, we are optimistic that we will not lose any significant investigation or case as a result of the loss of our building. No one whom we have sued or whose conduct we have been investigating should for a single moment doubt our resolve to continue our pursuit of justice in every such matter.

There also will not be any serious long-term impact on the Commission's oversight of securities firms located in the New York area. The Commission's records related to examinations of all securities firms are maintained electronically in a central database, and were unaffected by the tragedy. Electronic copies of examination reports and deficiency letters are maintained off-site for investment advisers, investment companies, broker-dealers and transfer agents. Records relating to open examinations will be reconstructed from records that exist at registrants' offices and from other sources. We are planning to utilize examination staff from other offices (Boston, Philadelphia and Washington, DC) and to work with self-regulatory organizations (the

NYSE and NASDR) to ensure that examination cycles are fulfilled and that appropriate examination oversight is maintained. We are very mindful of the disruption to many firms' operations and records, and are ensuring reasonable accommodation to requests for extensions of time for on-site examinations or to produce records and other information.

We also have brought our enforcement resources to bear in the wake of the September 11th attacks. Although any securities law violation is minor in relation to the atrocities perpetrated, we, along with other federal and state authorities, must canvass all possible evidence to identify the perpetrators. Because of the extraordinary circumstances of the current situation, we made an exception to our standard policy of not commenting on investigations. We, along with other U.S. and international authorities, are providing any assistance possible to the FBI as they track down those responsible for the heinous attacks.

The September 11th terrorist attacks also bring a new impetus to the Commission's, and the securities industry's, participation in the government's anti-money laundering efforts. I am confident that the securities industry and SROs stand as one with the Commission and our partners in government, including Congress, in the firm resolve to deny criminals the use of the nation's financial institutions, including broker dealers, to launder the proceeds of crime for profit, or for the furtherance of their criminal activities, including terrorism.

Commission staff announced this past May that it was conducting, along with the NYSE and NASD, an examination sweep to assess industry best practices for anti-money laundering compliance. While there may be some modification of timing to accommodate firms who are coping with the loss of employees, or whose records or systems are impaired, we expect these examinations to move forward to help shape our understanding of firm practices and challenges in the fight against money laundering.

As the Committee may already know, all but one of the Department of the Treasury's relevant reporting and record-keeping provisions under the basic anti-money laundering statute, the Bank Secrecy Act, have long applied to broker-dealers, and have been included within the Commission's and SROs' examination protocol. The 2001 National Money Laundering Strategy delivered to Congress last week by Treasury and the Department of Justice reports on progress being made to advance Treasury's remaining rulemaking, a rule requiring broker-dealers, like banks, to report suspicious transactions. We support extending suspicious activity reporting to broker-dealers, and have provided Treasury with comprehensive written comments and suggestions on how Treasury rules can address the challenges that confront the securities industry. It is helpful to note that even in the absence of a rule, for at least five years, a group of senior compliance personnel have met to share anti-money laundering approaches with one another, and with government. Our staff continues to be available to assist Treasury, and we look forward to the conclusion of the rulemaking process for broker-dealers.

We can be justifiably proud of our government and market participants and the way they have performed in this crisis. Everyone pulled together to overcome this disaster and successfully reopen the U.S. equities and options markets. We believe that much of the securities industry's success in meeting the demands of this unspeakable horror was due in part to the hard work and effort made to prepare for Y2K. Securities firms had in place contingency plans and emergency procedures designed to manage the conversion to 2000, which saw them through the events of September 11th. With the strength and insight we have gained from this crisis, we will move forward to make our markets even stronger, more transparent and more vibrant. In this way, we will honor the memory of those we lost. As a Nation, and as an agency, we cannot and will not allow terrorists to destroy our spirit or impede our mission.

On behalf of the Commission, I appreciate the opportunity to submit our views on the state of the Nation's securities markets in the wake of the recent terrorist attacks. I am happy to try to respond to any questions the Committee may have.